

INTRODUCTION

The Energy Users' Association of Australia (EUAA) is the peak body representing Australian commercial and industrial energy users. Our membership covers a broad cross section of the Australian economy including significant retail, manufacturing and materials processing industries. Combined, EUAA members employ over 1 million Australians, pay billions in energy bills every year and expect to see all parts of the energy supply chain making their contribution to the National Electricity Objective.

Our members are highly exposed to movements in both gas and electricity prices and have been under increasing stress due to escalating energy costs. These increased costs are either absorbed by the business, making it more difficult to maintain existing levels of employment or passed through to consumers in the form of increases in the prices paid for many everyday items.

Many of our members have significant operations in Victoria that employ thousands of people across the State. They are facing huge energy cost pressures as they seek to ensure the sustainability of their operations and their employees' livelihood.

The EUAA played a very active role in the recent comprehensive AEMC RERT review ("RERT Review")¹ that was only completed last May. We were supportive of the final AEMC rule change as an appropriate balance between reliability and cost. The RERT Review concluded:

"Crucially, the reliability standard is not zero per cent since this would be too costly for consumers. The reliability standard represents a trade-off between the prices paid for electricity and the cost of not having energy when it is needed: increasing levels of reliability involves increased costs." (para 36 pp. v-vi)

The RERT Review explicitly considered a multi-year RERT that was proposed by AEMO and the Victorian Government as part of the Review and which is now again being proposed by the Victorian Government in this current application. The Review concluded that:

"...the Commission considers that the increased costs for consumers would outweigh ...potential benefits..." (para 47 p.xi)

This submission focusses specifically on the issue of whether the derogation should be considered by way of an expedited rule change. A second submission will examine the merits of the derogation. The Victorian Government's arguments in favour of the expedited consideration seem to be:

- drawing on the August 2019 AEMO ESOO, there is evidence of material changes since May 2019 that mean the level of RERT that has already been contracted for Victoria in 2019/20 is insufficient
- the current information in MT PASA on generation availability cannot be relied upon and AEMO needs to be given additional power to contract RERT for 2019/20
- this additional RERT cannot be sourced from demand response as this has been exhausted which leaves small scale diesel and gas plant as the only provider; providers of this RERT require up to a three-year contract with associated guaranteed availability payments to offset the capital costs; this price is likely to be higher than the market price cap

¹ AEMC "Rule Determination National Electricity Amendment (Enhancement to the Reliability and Emergency Reserve Trader) Rule 2019" 2nd May 2019

- this new RERT can be put in place soon after 19th December to be available for the expected risks in January and February 2020

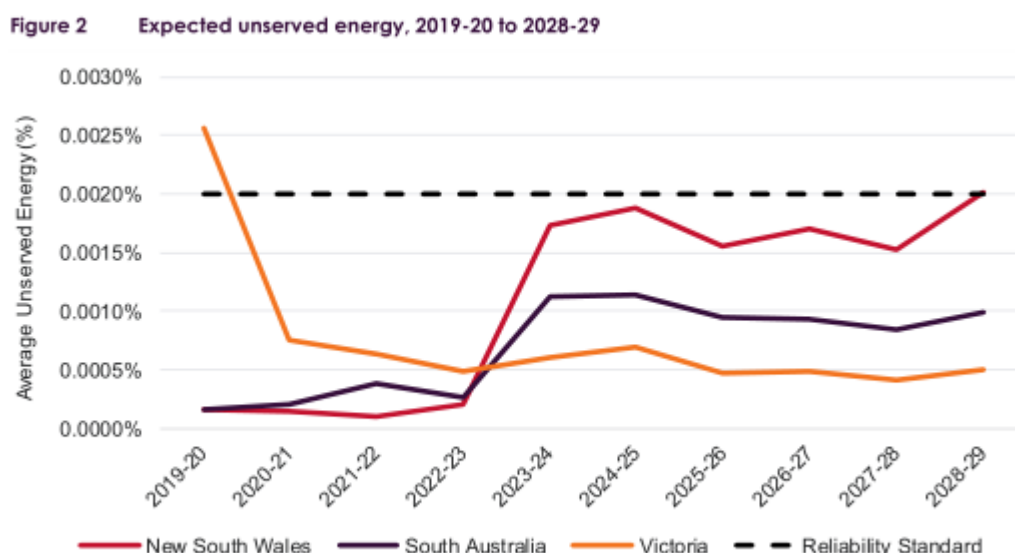
This submission responds to each of these issues and concludes that that the Victorian Government has not met the conditions for an expedited rule change as set out in s.87 of the NEL. Specifically, the Victorian Government has not provided sufficient evidence that it needs to procure additional RERT for 2019/20 so that:

“...the effective operation and administration of the wholesale electricity market and the reliability of the national electricity system as it operates in the state of Victoria, could be prejudiced or threatened, as there may be high reliability risks for the Victorian market during summer 2019-20.”²

We base our conclusion on the following arguments.

There has been a material change in conditions since the publication of the 2019 ESOO that means the level of expected USE in Victoria is now forecast to be below the reliability standard

The Victorian Government draws on the 21st August 2019 AEMO ESOO to support this argument. The ESOO concluded, in what they represented as the central case, that Victoria is likely to breach the 0.002% expected USE reliability standard in 2019/20 by 0.0006%.



This was driven by the assumed unavailability of two units of Torrens Island A power station in South Australia and an assumption that there was an 18% chance of both Loy Yang A2 and Mortlake 2 not being returned to service prior to 31st March 2020. The ESOO said that:

“Operation of these two units (Torrens Island) over summer would improve the reliability outlook for Victoria, reducing expected USE to 0.0020%, provided there is sufficient interconnector capacity available to import supply from South Australia. While this would just meet the reliability standard, large supply scarcity risks remain if either Mortlake or Loy Yang A2 outages are extended, or extreme weather conditions prevail.” (p.12)

We would argue that circumstances have materially changed since the publication of the ESOO:

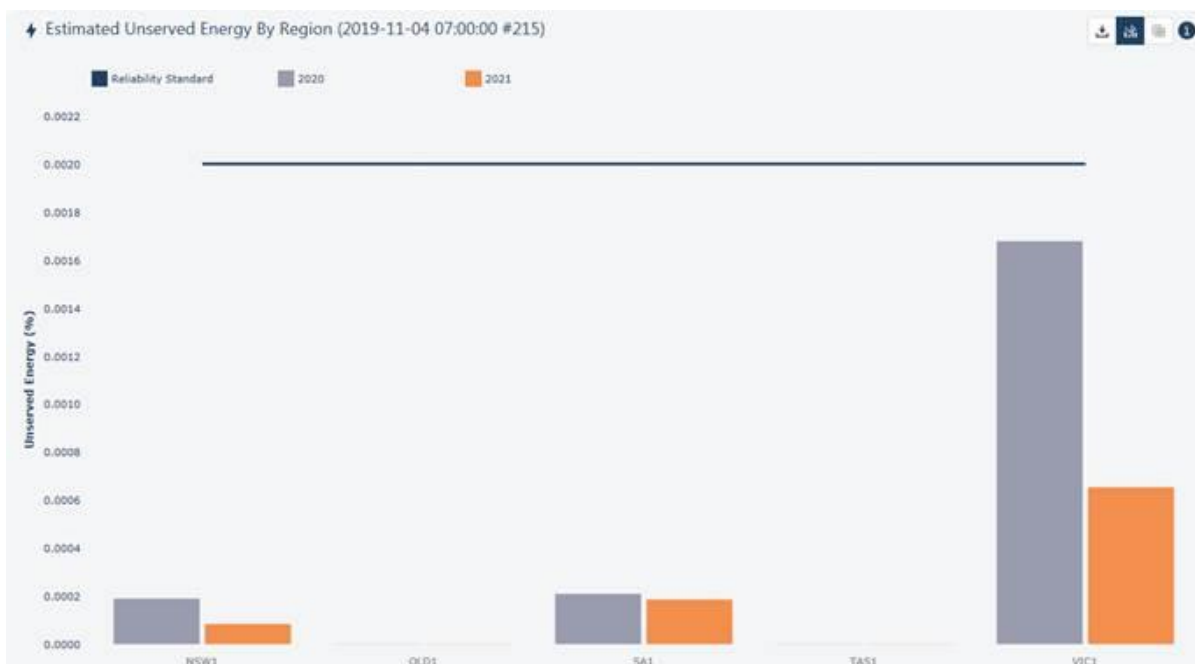
- The SA Government has confirmed that the two additional units at Torrens A will be operating³

² AEMC Consultation Paper p.24

³ Chris Russell “Old plant powers up for summer” Advertiser 24 October 2019 p.15

- The operators of both the Loy Yang A and Mortlake units have confirmed, in submission to the MT PASA, that they will be returning to service as scheduled, in December

The figure below shows the latest USE forecast for 2019/20 in MTPASA. The 0.0026 has been revised down to 0.00168 with 99% of the forecast USE associated with the conservative 10% POE demand forecast which based on historical outcomes has less than 1% probability of actually occurring.



While there may have been some debate on the assumptions AEMO developed in July/August for its ESOO modelling result that there was an 18% chance that neither Loy Yang A nor Mortlake would be available over the entire 2019/20 summer period⁴, we think it is reasonable to assume in early November that the information in MT PASA, which is updated by Origin and AGL on a weekly basis, should be relied on. MT PASA has these plants coming back on in December. As the AEMC RERT Review noted:

“Forecasting processes such as the medium-term PASA allow AEMO the flexibility to change its reliability assessments based on new information, including information about generation availability (e.g. whether a generator is out on maintenance or not) and changes in weather conditions. Participants are required to update the information they provide to AEMO every week and AEMO may change its inputs (e.g. its demand forecasts or its forced outage rates) if required as it learns new information – including updated weather conditions from the Bureau of Meteorology. AEMO updates the medium-term PASA weekly, using the latest available information. This makes sure that market participants, and AEMO, always make decisions based on the latest available and more accurate information.” (para 34 p. vi)

The Victorian government seems to doubt the accuracy of MTPSA data e.g. the comments on the unreliability of Victorian thermal plant.

“Victoria is in a unique position in the NEM in that it has a disproportionate dependence on a relatively small number of brown coal generation units, which are becoming increasingly unreliable...Unplanned outages appear to be increasing. The relative consequence of unplanned or forced outages of one or more coal-fired generation units is therefore greater for Victoria than any other jurisdiction...”

⁴ It is worth noting that there was no discussion with stakeholders on the AEMO assumptions on thermal plant availability prior to publication of the ESOO and the ESOO contained no information on how these assumptions were arrived at. That information only came nearly three weeks later and only after a specific request from the EUAA.

Victoria’s current, but transitioning, reliance on this ageing thermal baseload generation increases the State’s exposure to potential capacity shortage during periods of peak summer demand.” (pp 6-7)

However, we believe that it is important to emphasise the high standards of disclosure that AGL and Origin face in their reporting on the Loy Yang and Mortlake units in MTPASA.

- AGL and Origin are both publicly listed companies with duties of disclosure regarding material impacts on company performance and risk exposures
- AGL and Origin also participate in regulated financial markets when dealing in electricity derivatives, are Australian Financial Services Licence holders to support these activities, and face exposures under both Australian Financial Services and Australian Competition Laws with regard to conduct in markets
- There are civil penalty provisions addressing the provision of PASA data in cl 3.7.2 and 3.7.3 of the NER.
- Aside from their legal obligations, there will be significant reputational damage were their units not to come back on line as forecast.

Given, the significant legal risks associated with the provision of the poor quality PASA data, we think it reasonable to assume that the engineering and management assessments informing the provision of information into MT PASA are rigorous and would expose senior and executive managers to significant risks if deliberately misleading or negligent.

So, when we see the statement by the AGL Chief Executive Brett Redman as recently as the 4th November, at the opening of the Barker Inlet gas fired power station in South Australia:

“We’re confident that our unit at Loy Yang will be back up and running as scheduled on December 16.”⁵

We have no reason to disbelieve him.

It is reasonable to assume AEMO has already procured RERT contracts to cover the expected USE risk identified in 2019 ESOO

The Government comments:

“If Victoria were to experience another extreme heatwave that drove one-in-10-year peak demand, the expected USE would rise to an unprecedented 0.0148%, over seven times the current reliability standard. To manage an event like this, AEMO would be required to load shed the equivalent of between 260,000 and 1.3 million households in Victoria for four hours, typically during extreme temperatures or heatwaves.” (p. 5)

And later says:

“...the worst case of neither unit being available and Victoria experiencing a one-in-10-year peak demand, USE could jump to 0.0148% over the 2019-20 summer peak demand period.

Yet this is not new news. It was clearly set out on page 1 of the Executive Summary in the 2019 ESOO. Given that AEMO would have consulted with the Victorian Government on the level of short, medium and long notice RERT that AEMO should contract for 2019/20, we think it is reasonable to assume that these extreme circumstances – including the Government’s worst-case scenario, would have been considered in the level of RERT that has already been pre-negotiated or contracted. AEMO has not issued any statements since its initial invitation to bid for RERT that indicate that it has failed to procure sufficient RERT e.g. “we are seeking additional RERT as we have been unable to contract enough in the first round of offers”.

⁵ “State gas ban puts grid at risk: Taylor” Australian 5th November 2019 p.20
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It is unfortunate that AEMO has not announced the level of short, medium and long notice RERT that has been pre-negotiated to assist stakeholders to more transparently assess this derogation application.

Yet the Government seems to argue that whatever the level that has been contracted, it is insufficient:

“Given implications for reliability during summer 2019-20, this rule change request relates to a matter that, if not made as a matter of urgency, will result in an inability to contract sufficient RERT reserve capacity over the peak summer demand period in 2019-20 which will imminently prejudice or threaten the reliability of the national electricity system as it operates in Victoria.” (p. 3)

So despite what MTPASA is saying, despite the legal and reputational consequences of Origin and AGL of not putting in the correct information, despite what the AGL CEO is saying, despite the South Australian Government’s decision on Torren A, despite Victorian Government discussions with AEMO on the level of RERT to be purchased based on the 2019 ES00, despite AEMO giving no indication that the level of RERT they have already contracted for in 2019/20, the Victorian Government still want AEMO to be able to buy more RERT – in the form of strategic reserves - for 2019/20 and a further two years. The cost of which will all be borne by consumers in Victoria.

We are not satisfied that the purchase of additional RERT for 2019/20 meets the NEO

The Government argues that given:

“indications are that maximum market availability for demand-side contracts has been materially reached” (p.6)

any additional RERT for 2019/20 would be the:

“...type of supply would most likely be supplied by small-scale gas and diesel generation.” (p.6)

which would be acquired under a three-year contract where the provider is paid an availability payment to cover their costs.

We do not believe this approach meets the NEO i.e. promotes reliability having regards to costs and benefits, minimised market distortions and minimises direct costs.

The purchase of this form of additional RERT for 2019/20 and beyond increases market distortions

The application argues:

“The derogation will not adversely impact investment in the NEM, given its limited scale and duration (to 2025).” (p.8)

We have interpreted “not adversely impact investment in the NEM” as “not adversely impacting on the availability of ‘in-market’ reserves”. The RERT Review described it as:

“Reliability outcomes in the NEM are largely driven by market participants making investment and operational decisions, taking into account expectations and information that is provided on future demand and supply. Generators and retailers have strong financial incentives to provide in-market reserves in order to support the operation of the power system in a reliable manner.” (para 7, p. ii)

“As part of the broader reliability standard, the RERT is a safety net, a last resort mechanism to use when the other elements have been exhausted. It is not a primary mechanism for meeting reliability. This is the role of the market. This is further reinforced by the introduction of the retailer reliability obligation, which builds on existing spot and financial market arrangements in the NEM to facilitate investment in dispatchable capacity and demand response in order to support the reliability of the power system.” (para 10 p.11 – emphasis added)

“The core objective of the existing reliability framework in the NEM is to deliver desired reliability outcomes through market mechanisms to the largest extent possible. In a reliable power system, the expected level of supply in the market will include a buffer, known as in market reserves. Expected supply will be greater than expected demand. In the event that the supply / demand balance tightens, spot and contract prices would rise, which will inform operational decisions and provide an incentive for entry and expansion, addressing any potential reliability problems as or before they arise. This allows the actual demand and supply to be kept in balance, even in the face of shocks to the system. (para 30 p. v)

So RERT is a safety net and is directly linked to the reliability standard. It is only required after all in-market reserves are exhausted. We submit that purchasing strategic reserves for 2019/20 and a further 2 years distorts the market. Given that there is very little time post 19th December to source the additional RERT, it must come from plant that is already “in-market” or potentially “in-market”. Taking this generation out of the market to put it in RERT distorts the market which adds inefficient costs to consumers bills.

The purchase of this form of additional RERT in 2019/20 and beyond does not have regard to efficient costs to benefits

In its rejection of standing reserves, the RERT Review recognised that while they:

“... could potentially result in cheaper emergency reserves being provided, the Commission considers that the increased costs for consumers would outweigh these potential benefits since:

- *Consumers would pay for emergency reserves every year regardless of whether or not the emergency reserves are required – thereby increasing electricity costs.*
- *In addition, allowing standing reserves would likely disincentivise investment in all forms of generation (and demand response) in the market which would lead to higher wholesale market prices – further increasing costs to consumers.” (para 47 p x-xi)*

Fundamental to an efficient NEM outcome that is consistent with the NEO is for reserves to as much as possible to be in-market because the maximum cost to consumers is the market price cap.

Yet the Government seems to regard additional RERT contracted under 3-year contracts as attractive because they can be supplied at a price lower than the value of customer reliability:

“Based on preliminary discussions with potential RERT supply side providers, the Department of Environment, Land, Water and Planning (DELWP) is aware that several parties have stated that they are unable to offer in resources below the value of customer reliability within the constraints of a one-year RERT contract. However, these same parties have indicated that they are able to provide substantial new energy generation resources at significantly lower annual cost if multi-year contracts were available.” (p.6)

We are not surprised that potential RERT providers are happy to step up when they are guaranteed a three-year availability payment to cover their capital costs with that payment well above the market price cap. Much more preferable to taking their chances in the spot market. But that is what leads to the market distortions and higher than efficient costs to consumers. Offering to pay these generators above the MPC means they are happy to go out of the market and into RERT when the efficient market outcome for consumers is that they stay in-market.

The Government seems confident that if it gets the rule change approved by 19th December it will quickly be able to source strategic reserves it claims are required for 2019/20 summer. In the absence of any detail about how this process might work in the Government’s application, we can only conclude that discussions have been held and indicative commitments made.

It that is the case it seems that the Government is wanting to bring reserves out of the market and into RERT for 2019/20 even if the cost to consumers is multiple times the market price cap. This does not meet the NEO test. Not

only are consumers stuck with these costs in 2019/20, but also for the subsequent years irrespective of whether the RERT is required. This does not meet the NEO test.

Please contact me if you would like to discuss this submission further.

Sincerely,

A handwritten signature in black ink, appearing to read 'A Richards', written in a cursive style.

Andrew Richards
Chief Executive Officer